Prosperity Bancshares Inc. (PB)

Updated August 16th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	$77	**5 Year CAGR Estimate:**	7.7%	**Market Cap:**	$7.0 B
Fair Value Price:	$82	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	9/16/2022
% Fair Value:	94%	**5 Year Valuation Multiple Estimate:**	1.1%	**Dividend Payment Date:**	10/3/2022
Dividend Yield:	2.7%	**5 Year Price Target**	$99	**Years Of Dividend Growth:**	18
Dividend Risk Score:	B	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

Prosperity Bancshares Inc. was formed in 1983 as a vehicle to acquire the former Allied Bank - chartered in 1949 as the First National Bank of Edna, Texas - which is now known as Prosperity Bank. The bank's main operation is receiving deposits from the general public and using the capital to originate commercial and consumer loans. The bank operates 261 branches in the greater Houston area and some neighboring counties in Texas and 14 more branches in Oklahoma. The company also has the following operations: wealth management, retail brokerage, and mortgage banking investment services. The bank's main lending focus is commercial mortgages, which make up 33% of their loan portfolio, followed by residential mortgages, which make up 24%. The company has a market capitalization of $7.0 billion.

On November 1st, 2019, Prosperity Bancshares completed the acquisition of LegacyTexas Bank in a deal valued at $2.1 billion. LegacyTexas has 42 branches in Texas and thus it has strengthened the position of Prosperity Bancshares in the area. As the deal value of $2.1 billion was almost half of the market cap of Prosperity Bancshares before the deal, it is evident that this acquisition is major for the future growth of Prosperity.

In late July, Prosperity Bancshares reported (7/27/22) financial results for the second quarter of fiscal 2022. Deposits decreased -4% sequentially due to lower public fund deposits but non-performing loans remained low, at 0.07% of interest-earning assets, and loans grew 2.4%. Given also higher interest rates, the bank grew its earnings-per-share 5% sequentially, from $1.33 to $1.40. Even better, it expects continued earnings growth thanks to rising interest rates. Thanks to strong business momentum, we have raised our annual forecast from $5.50 to $5.70. Prosperity Bancshares has a reputation for its disciplined management and thus it has easily endured the pandemic and low interest rates. Its record earnings in 2020-2021 and its dividend raises in 2020 and 2021 are testaments to its resilience to downturns.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$3.23	$3.65	$4.32	$4.09	$3.94	$3.92	$4.61	$4.52	$5.68	$5.60	***$5.70***	***$6.93***
DPS	$1.00	$0.65	$0.99	$1.12	$1.24	$1.38	$1.49	$1.64	$1.87	$1.99	***$2.08***	***$2.76***
Shares[1]	56.5	66.1	69.8	70.0	69.5	69.5	69.9	94.7	92.6	92.2	***91.0***	***90.0***

Prosperity Bancshares has grown its earnings-per-share at a 6.3% average annual rate in the last decade, primarily thanks to strong economic activity in Texas and Oklahoma. Texas has the fastest-growing population and one of the highest economic growth rates in the nation. It is also expected to outperform most other states in economic growth over the next three years. Prosperity Bancshares stalled from 2014 to 2017 but it has reignited growth in the last five years. In addition, the pandemic has not disrupted the growth trajectory of the bank, primarily thanks to its recent major acquisition and the resultant synergies. Moreover, the Fed has begun to raise interest rates aggressively this year and thus it will provide a tailwind to the entire financial sector. Due to the nearly all-time high earnings in 2021, we expect the bank to grow its earnings-per-share by 4.0% per year on average over the next five years. The bank initiated a quarterly dividend of $0.025 per share in January-1999 and has grown it at a fast clip to $0.52 per quarter. In the last five

[1] In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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years, the bank has raised its dividend by 8.9% per year on average. Thanks to its low payout ratio (36%) and its promising growth prospects, it should be able to continue raising its dividend at a healthy pace.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	12.7	17.2	12.9	11.8	18.3	17.7	13.5	15.4	10.5	13.0	***13.5***	***14.3***
Avg. Yld.	2.3%	1.2%	1.7%	2.1%	2.4%	2.1%	2.1%	2.4%	3.1%	2.7%	***2.7%***	***2.8%***

Prosperity Bancshares is currently trading at a price-to-earnings ratio of 13.5, which is slightly lower than its 10-year average earnings multiple of 14.3. If the stock trades at its average valuation level in five years, it will enjoy a 1.1% annualized gain in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	25%	24%	23%	27%	31%	35%	32%	36%	33%	36%	***36%***	***40%***

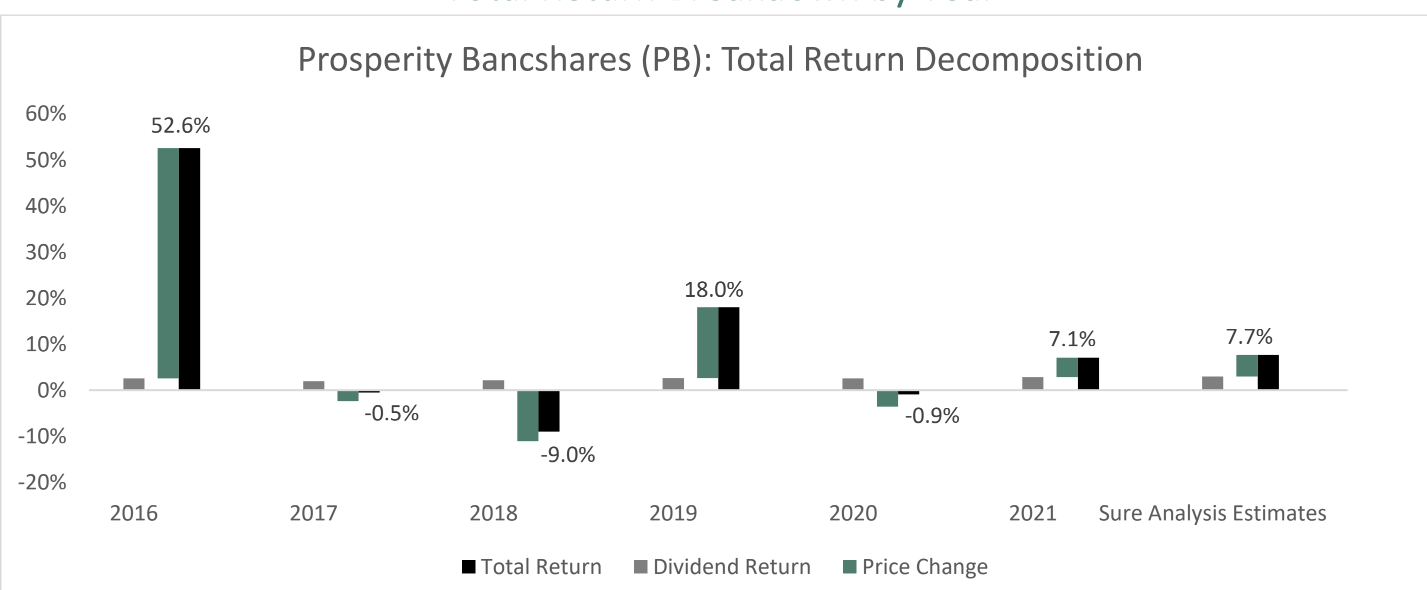
Prosperity Bancshares believes that its competitive advantage is in its presence in areas with strong economic growth and excellent growth opportunities through acquisitions, new banking center locations and business development.

Moreover, Prosperity Bancshares has proved resilient to recessions. In the coronavirus crisis, the bank managed to post record earnings-per-share. In addition, the bank was able to grow immensely in the previous recession. During the Great Recession (2008-2009), its stock rallied 36% throughout the year despite a declining broad market. The company was also able to grow its earnings-per-share by an outstanding 29% and its book value per share by nearly 7%.

Final Thoughts & Recommendation

Prosperity Bancshares is conservatively managed and has endured the pandemic without any problem. Thanks to rising interest rates, which are likely to help the bank expand its net interest margin, the stock has rallied 17% since our last research report and hence it has become somewhat less attractive. We now expect the stock to offer a 7.7% average annual return over the next five years and hence we have lowered our rating from "buy" to "hold". Nevertheless, we remain enthused over the long-term prospects of this high-quality bank.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	447	582	776	736	734	716	728	796	1,122	1,098
SG&A Exp.	138	177	236	228	232	227	241	256	343	344
D&A Exp.	16	17	24	22	22	19	18	20	31	30
Net Profit	168	221	297	287	274	272	322	333	529	519
Net Margin	37.6%	38.0%	38.3%	39.0%	37.4%	38.0%	44.2%	41.8%	47.1%	47.3%
Free Cash Flow	197	284	336	301	329	379	305	384	560	676
Income Tax	84	108	148	144	134	134	81	87	116	140

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	14,584	18,642	21,508	22,037	22,331	22,587	22,693	32,186	34,059	37,834
Cash & Equivalents	326	381	677	563	436	392	411	574	1,343	2,548
Accounts Receivable	42	49	52	52	53	56	57	81	82	66
Goodwill & Int. Ass.	1,243	1,714	1,933	1,918	1,947	1,940	1,934	3,310	3,305	3,293
Total Liabilities	12,494	15,855	18,263	18,574	18,689	18,763	18,641	26,215	27,929	31,407
Accounts Payable	2	3	3	2	2	3	4	9	3	1
Long-Term Debt	342	135	176	491	991	505	1,031	1,430	---	---
Shareholder's Equity	2,089	2,787	3,245	3,463	3,642	3,824	4,053	5,971	6,131	6,427
LTD/E Ratio	0.16	0.05	0.05	0.14	0.27	0.13	0.25	0.24	---	---

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	1.4%	1.3%	1.5%	1.3%	1.2%	1.2%	1.4%	1.2%	1.6%	1.4%
Return on Equity	9.2%	9.1%	9.9%	8.5%	7.7%	7.3%	8.2%	6.6%	8.7%	8.3%
ROIC	8.2%	8.3%	9.4%	7.8%	6.4%	6.1%	6.8%	5.3%	7.8%	8.3%
Shares Out.	56.5	66.1	69.8	70.0	69.5	69.5	69.9	94.7	92.6	92.2
Revenue/Share	8.60	9.61	11.26	10.50	10.53	10.31	10.42	10.83	12.06	11.85
FCF/Share	3.80	4.68	4.88	4.30	4.73	5.46	4.37	5.23	6.02	7.29

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.